

ORIGINAL



0000151648

RECEIVED

FENNEMORE CRAIG, P.C.
Jay L. Shapiro (No. 014650)
2394 East Camelback Road
Suite 600
Phoenix, Arizona 85016

2014 MAR - 1 P 4: 27

Arizona Corporation Commission

DOCKETED

MAR 07 2014

ARIZONA CORPORATION COMMISSION
DOCKET CONTROL

Attorneys for Lago Del Oro Water Company

DOCKETED BY

BEFORE THE ARIZONA CORPORATION COMMISSION

IN THE MATTER OF THE APPLICATION
OF LAGO DEL ORO WATER COMPANY,
AN ARIZONA CORPORATION, FOR
AUTHORITY TO: (1) ISSUE EVIDENCE OF
INDEBTEDNESS IN AN AMOUNT NOT TO
EXCEED \$3,900,000 IN CONNECTION
WITH THE PURCHASE OF EQUITY; AND
(2) ENCUMBER REAL PROPERTY AND
PLANT AS SECURITY FOR SUCH
INDEBTEDNESS.

DOCKET NO: W-01944A-13-0242

**LAGO DEL ORO WATER
COMPANY'S POSITION
STATEMENT REGARDING
CONSOLIDATION**

Pursuant to the Procedural Order issued on February 28, 2014, Lago Del Oro Water Company ("LDO" or the "Company") hereby submits its position statement regarding consolidation of its rate application (Docket No. W-01944A-13-0215) with its financing application.

LDO's current capital structure is 100 percent equity. As stated in the Company's financing application, the purpose of the financing is "to rebalance LDO's capital structure."¹ The rebalancing of the Company's capital structure will be accomplished by using the debt financing to reimburse shareholders for the recent purchase of a portion of LDO's utility plant put into service between 1997 and 2009, but only purchased in 2012. The proposed rebalancing results in a new capital structure that is "more balanced," closer to the typical capital structures of the cost of capital proxy companies, and it "favors

¹ Financing Application at 2:25.

1 customers as the cost of debt is less than the cost of equity.²

2 The Company's request for financing and associated capital structure rebalancing
3 represents good business practice and is appropriate, whether or not LDO ultimately
4 increases its rates. This is why the Company did not link its financing request to the rate
5 case and why Staff has evaluated the Company's financing application without
6 consideration of increased rates that may or may not be granted. Although there is
7 interconnection of issues between the financing case and the rate case, consolidation is not
8 required to address the interconnections.

9 The first interconnection is the capital structure itself. As noted, a more balanced
10 capital structure results in lower rates for customers. The linking between capital
11 structure and rates is purely mathematical, and addressing this linkage is made easier by
12 separation of the financing case and rate case. Once the financing case is complete,
13 the Company can complete the loan and the Company's cost of debt can be accurately
14 incorporated into calculating the Company's weighted average cost of capital and revenue
15 requirement in the rate case. In contrast, in a consolidated case, the Company will not
16 complete the financing until well after the issuance of a rate order, which could result in a
17 mismatch between the proforma interest rate used in the rate case and the actual interest
18 rate incurred by the Company.

19 As previously noted, the Company believes there is significant risk of interest rate
20 increases or, in an extreme circumstance, a complete loss of the ability to finance the
21 transaction as the rate case proceeds. Given the current favorable interest rates and
22 financing terms available to the Company, and the fact that completing the financing
23 outside of the rate case results in debt cost certainty and increased accuracy in calculating
24 the Company's weighted cost of capital and resulting revenue requirement, the Company

25

26 ² See *Id.* at 3:6.

1 does not see a good reason to consolidate the cases to address cost of capital linkage,
2 and there is risk that linking of the cases will result in higher customer rates due to an
3 increase in interest rates.

4 The second relationship between the cases is that the financing proceeds will be
5 used to reimburse shareholders for the purchase of a portion of LDO's utility plant put into
6 service between 1997 and 2009 and purchased in 2012. The Company believes at this
7 point in the processing of both cases, the linkage is inconsequential.

8 In terms of the financing application, the recent plant purchase was used as a basis
9 to determine an appropriate amount of financing to be issued. Due to the delayed
10 purchase of the plant, Staff has recommended that adjustments be made to reduce rate
11 base to account for the intervening depreciation of the plant and that the financing be
12 reduced to the net plant value of the recently purchased assets. The Company and Staff
13 are in agreement as to the calculation of intervening accumulated depreciation and the
14 resulting net plant value and rate base, and the Company has agreed to Staff's
15 recommendation to limit its financing to the net plant value.³ Since the net plant
16 calculation is purely mathematical, there is no chance that the net plant value of the
17 purchased assets will change as the rate case proceeds. Therefore, there is no remaining
18 linkage between the plant purchase's net plant value and the financing application that
19 needs to be addressed in a consolidated docket.⁴

20 In taking this position, that consolidation is not warranted, the Company is mindful
21 that Judge Rodda and/or the Commission may have questions about the financing, its

22 ³ See Staff Report at 2-3; LDO Response to Staff Report.

23 ⁴ There are remaining differences between the Company and Staff in the calculation of
24 depreciation expense related to the purchased plant. However, the disputed depreciation
25 expense results in relatively small differences in the overall revenue requirement. These
26 differences in depreciation expense and revenue requirement positions do not in any way
impact the Company's financing request because Staff's financing recommendation is
based on current rates and does not consider any increase that will result from the rate
case.

1 impact on the rates, and about rate base. The Company will be prepared to answer those
2 questions in each docket as they come up. However, given that Staff and the Company
3 are in agreement on the financing, the consolidation, and the amount of the recently
4 purchased plant that goes into rate base, there seems little reason to risk that the Company
5 could lose the current financing or otherwise have to pay more for the debt.

6 RESPECTFULLY SUBMITTED this 7th day of March, 2014.

7 FENNEMORE CRAIG, P.C.
8 

9 By _____

Jay L. Shapiro
2394 East Camelback Road, Suite 600
Phoenix, Arizona 85016
Attorneys for Lago Del Oro Water
Company

1 ORIGINAL and thirteen (13) copies
2 of the foregoing were delivered
this 7th day of March, 2014, to:

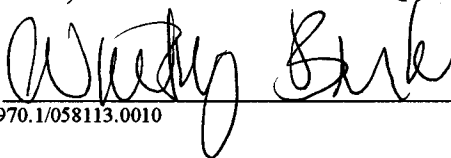
3 Docket Control
4 Arizona Corporation Commission
1200 W. Washington St.
5 Phoenix, AZ 85007

6 COPY of the foregoing was emailed/mailed
this 7th day of March, 2014, to:

7 Jane Rodda, ALJ
8 Hearing Division
Arizona Corporation Commission
400 West Congress
9 Tucson, AZ 85701

10 COPY of the foregoing was hand-delivered
11 this 7th day of March, 2014, to:

12 Robin Mitchell, Esq.
Legal Division
13 Arizona Corporation Commission
1200 W. Washington St.
14 Phoenix, AZ 85007

15 By: 
16 8964970.1/058113.0010

17
18
19
20
21
22
23
24
25
26